

Tennessee Regulatory Authority

**For the Year Ended
June 30, 1997**

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November 18, 1998

The Honorable Don Sundquist, Governor
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and

The Honorable Melvin Malone, Chairman
The Honorable Lynn Greer, Director
The Honorable Sara Kyle, Director
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, Tennessee 37243-0505

Ladies and Gentlemen:

We have conducted a financial and compliance audit of selected programs and activities of the Tennessee Regulatory Authority for the year ended June 30, 1997.

We conducted our audit in accordance with generally accepted government auditing standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. These standards require that we obtain an understanding of management controls relevant to the audit and that we design the audit to provide reasonable assurance of the authority's compliance with the provisions of laws, regulations, contracts, and grants significant to the audit. Management of the Tennessee Regulatory Authority is responsible for establishing and maintaining internal control and for complying with applicable laws and regulations.

Our audit disclosed a finding which is detailed in the Objectives, Methodologies, and Conclusions section of this report. The authority's administration has responded to the audit finding; we have included the response following the finding. We will follow up the audit to examine the application of the procedures instituted because of the audit finding.

We have reported other less significant matters involving the authority's internal controls and/or instances of noncompliance to the Tennessee Regulatory Authority's management in a separate letter.

Very truly yours,

W. R. Snodgrass
Comptroller of the Treasury

State of Tennessee

Audit Highlights

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit
Tennessee Regulatory Authority
For the Year Ended June 30, 1997

AUDIT SCOPE

We have audited the Tennessee Regulatory Authority for the period July 1, 1996, through June 30, 1997. Our audit scope included a review of management's controls and compliance with policies, procedures, laws, and regulations in the areas of revenues, expenditures, equipment, payroll and personnel, and compliance with the Financial Integrity Act. The audit was conducted in accordance with generally accepted government auditing standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

AUDIT FINDING

Noncompliance with the Financial Integrity Act*

The authority did not prepare and submit the Financial Integrity Act report which was due December 31, 1997 (page 6).

* This finding is repeated from the prior audit.

"Audit Highlights" is a summary of the audit report. To obtain the complete audit report which contains all findings, recommendations, and management comments, please contact

Comptroller of the Treasury, Division of State Audit
1500 James K. Polk Building, Nashville, TN 37243-0264
(615) 741-3697

**Audit Report
Tennessee Regulatory Authority
For the Year Ended June 30, 1997**

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Tennessee Regulatory Authority For the Year Ended June 30, 1997

INTRODUCTION

POST-AUDIT AUTHORITY

This is the report on the financial and compliance audit of the Tennessee Regulatory Authority. The audit was conducted pursuant to Section 4-3-304, *Tennessee Code Annotated*, which authorizes the Department of Audit to “perform currently a post-audit of all accounts and other financial records of the state government, and of any department, institution, office, or agency thereof in accordance with generally accepted auditing standards and in accordance with such procedures as may be established by the comptroller.”

Section 8-4-109, *Tennessee Code Annotated*, authorizes the Comptroller of the Treasury to audit any books and records of any governmental entity that handles public funds when the Comptroller considers an audit to be necessary or appropriate.

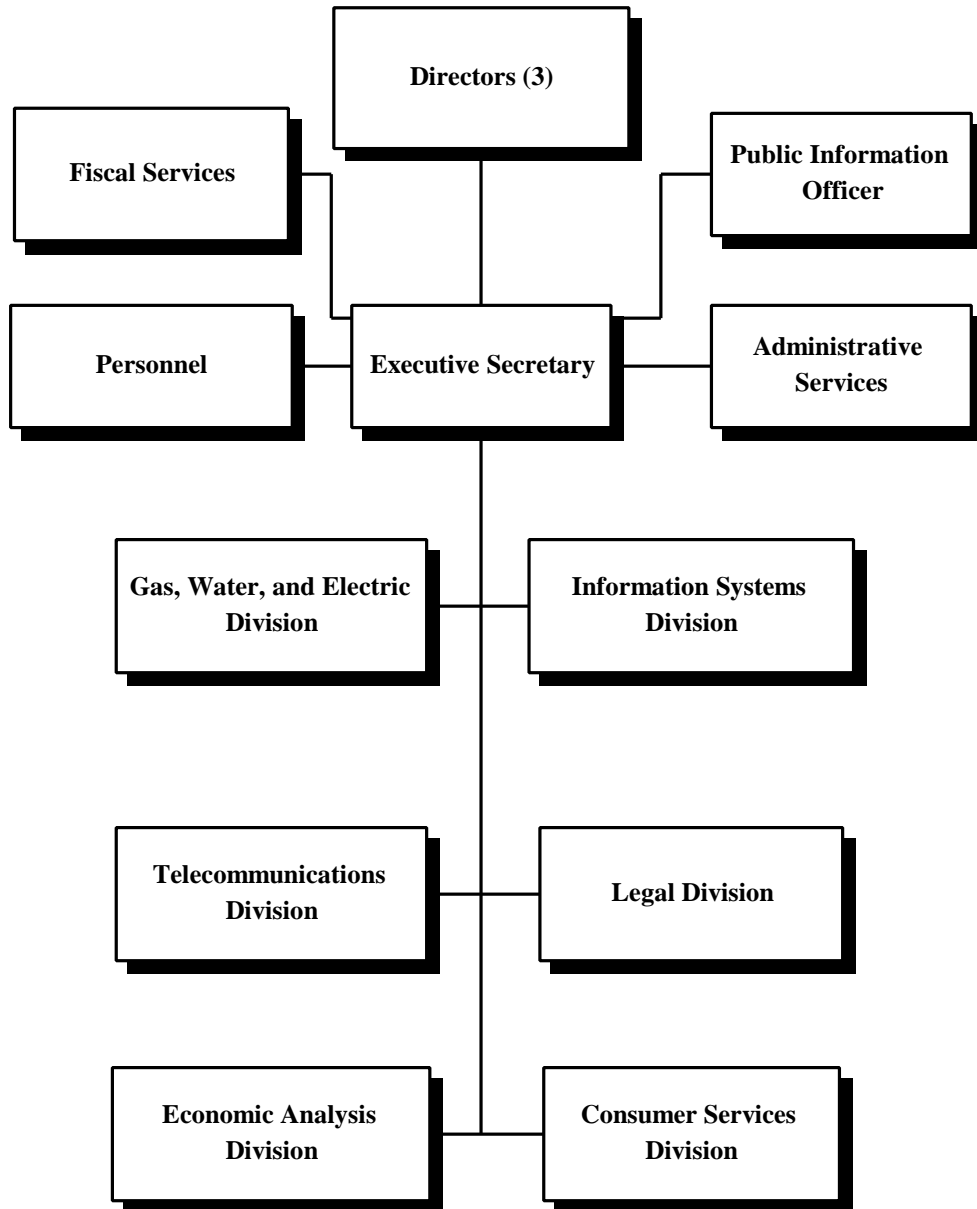
BACKGROUND

The Tennessee Regulatory Authority is governed by three directors. One is appointed by the Governor, one by the Speaker of the Senate, and one by the Speaker of the House of Representatives. Each director serves a six-year term. The authority has jurisdiction over public utilities including electric companies, telephone companies, water companies, and natural gas companies. This jurisdiction includes approving all rates; auditing the utilities’ compliance with applicable laws, orders, and policies of the authority; and inspecting natural gas pipelines. An organization chart of the authority is on the following page.

AUDIT SCOPE

We have audited the Tennessee Regulatory Authority for the period July 1, 1996, through June 30, 1997. Our audit scope included a review of management’s controls and compliance with policies, procedures, laws, and regulations in the areas of revenues, expenditures, equipment, payroll and personnel, and compliance with the Financial Integrity Act. The audit was conducted in accordance with generally accepted government auditing standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**TENNESSEE REGULATORY AUTHORITY
ORGANIZATION CHART**



OBJECTIVES, METHODOLOGIES, AND CONCLUSIONS

REVENUES

The objectives of our review of revenues controls and procedures were to determine whether

- transactions were recorded accurately in the accounting records and were properly documented,
- cash collected during the audit period was deposited timely and accounted for in the appropriate fiscal year,
- receipts were issued for all cash received,
- cash-receipting duties were properly segregated, and
- financial records were reconciled with the State of Tennessee Accounting and Reporting System (STARS).

We interviewed key personnel to gain an understanding of the authority's procedures and controls over revenues. We also reviewed supporting documentation and tested samples of revenue transactions. We had no findings related to revenues; however, other minor weaknesses came to our attention and were reported to management in a separate letter.

EXPENDITURES

The objectives of our review of expenditures controls and procedures were to determine whether

- expenditures were for goods or services received during the fiscal year;
- expenditures for goods or services were properly recorded in STARS;
- expenditures for goods or services were properly approved and in accordance with the budget and other regulations or requirements;
- expenditures for goods or services were recorded for the correct allotment code, cost center, transaction code, object code, budget category, and amount;
- payments were made within 45 days of the receipt of the invoice;
- accounting records were reconciled with STARS;
- expenditures for travel were in accordance with regulations;
- contracts were made in accordance with regulations;
- contract payments complied with contract terms and purchasing guidelines;

- encumbered funds were liquidated for the same purpose as the original encumbrance; and
- access to STARS and the Tennessee On-Line Purchasing System (TOPS) was limited to those persons whose job duties required it.

We interviewed key personnel to gain an understanding of the authority's procedures and controls over expenditures. We also reviewed supporting documentation and tested samples of expenditure transactions. In addition, we reviewed listings of staff who had access to STARS and TOPS. We had no findings related to expenditures; however, other minor weaknesses came to our attention and were reported to management in a separate letter.

EQUIPMENT

The objectives of our review of equipment controls and procedures were to determine whether

- property and equipment in the Property of the State of Tennessee (POST) system represented a complete and valid listing of the cost of assets purchased and physically on hand;
- costs associated with sold, abandoned, damaged, or obsolete fixed assets had been removed from POST;
- property and equipment were adequately safeguarded; and
- equipment leased from the Office for Information Resources (OIR) was properly accounted for.

We interviewed key personnel to gain an understanding of the authority's procedures and controls over equipment. We also reviewed supporting documentation and tested samples of equipment transactions. We had no findings related to equipment; however, other minor weaknesses came to our attention and were reported to management in a separate letter.

PAYROLL AND PERSONNEL

The objectives of our review of payroll and personnel controls and procedures were to determine whether

- payroll disbursements were made only for work authorized and performed;
- payroll was computed using rates and other factors in accordance with contracts and relevant laws and regulations;
- payroll was recorded correctly as to amount and period and was distributed properly to account, fund, and budget;

- employees were qualified for their positions;
- performance evaluations were completed in the time period required;
- temporary employees who were retirees of the Tennessee Consolidated Retirement System were employed in compliance with Section 8-36-805, *Tennessee Code Annotated*;
- access to the State Employee Information System (SEIS) was limited to those persons whose job duties required it;
- payroll and personnel duties were adequately segregated; and
- payroll changes were properly approved.

We interviewed key personnel to gain an understanding of the authority's procedures and controls over payroll and personnel. We also reviewed supporting documentation and tested samples of payroll and personnel. We had no findings related to payroll and personnel; however, other minor weaknesses came to our attention and were reported to management in a separate letter.

FINANCIAL INTEGRITY ACT

The Financial Integrity Act of 1983 requires each executive agency to annually evaluate its systems of internal accounting and administrative control and report the results of its evaluation to the Commissioner of Finance and Administration and the Comptroller of the Treasury by December 31 of each year.

The objectives of our review of the Tennessee Regulatory Authority's compliance with the Financial Integrity Act were to determine whether

- the authority's reports were filed in compliance with the Financial Integrity Act of 1983,
- documentation to support the authority's evaluation was properly maintained,
- procedures used in compiling information for the reports were adequate, and
- corrective actions were implemented for weaknesses identified in the reports.

We interviewed key employees responsible for compiling information for the reports to gain an understanding of the procedures. We also reviewed the supporting documentation for these procedures and the reports submitted to the Comptroller of the Treasury and to the Department of Finance and Administration.

We determined that the Financial Integrity Act report due on December 31, 1996, was submitted on time, and support for the report was adequate. However, the report due December 31, 1997, was not completed and submitted, as discussed in the following finding.

The authority did not comply with the Financial Integrity Act

Finding

As stated in the final audit report of the Public Service Commission, predecessor to the Tennessee Regulatory Authority, the authority did not comply with the Financial Integrity Act. Management concurred with the prior finding and indicated that a new internal audit team headed by a Utility Rate Manager had been assigned the tasks outlined in the act. Although a report documenting the authority's evaluation of its system of internal accounting and administrative control was filed for the year ended December 31, 1996, the agency did not complete a review or submit a report for the year ended December 31, 1997.

Section 9-18-102, *Tennessee Code Annotated*, stipulates:

Each agency of state government shall establish internal accounting and administrative controls which shall provide reasonable assurance that:

- (1) Obligations and costs are in compliance with applicable law;
- (2) Funds, property and other assets are safeguarded against waste, loss, unauthorized use or misappropriation; and
- (3) Revenues and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over the assets.

Section 9-18-104, stipulates:

- (a) By December 31 of each year, the head of each executive agency shall, on the basis of an evaluation conducted in accordance with guidelines prescribed under the preceding section, prepare and transmit to the commissioner of finance and administration and the comptroller of the treasury a report which states that:
 - (1) The agency's systems of internal accounting and administrative control fully comply with the requirements specified in this chapter; or
 - (2) The agency's systems of internal accounting and administrative control do not fully comply with such requirements.

- (b) In the event that the agency's systems do not fully comply with such requirements, the report shall include and identify any material weaknesses in the agency's systems of internal accounting and administrative control and the plans and schedule for correcting such weaknesses.

The Department of Finance and Administration has established guidelines for agencies to follow in evaluating their systems' compliance with the above requirements. An annual evaluation of internal accounting and administrative controls is needed to provide reasonable assurance that obligations and costs comply with applicable laws, assets are safeguarded, and revenues and expenditures are properly recorded and accounted for.

Recommendation

The chairman of the authority should assign someone responsibility for evaluating the systems of internal accounting and administrative control as required by Section 9-18-102, *Tennessee Code Annotated*. This person should report directly to the chairman. The chair should set deadlines for the completion of each step of the evaluation process and should ensure these deadlines are met. A report detailing the results of the examination should be submitted to the Commissioner of Finance and Administration and the Comptroller of the Treasury or regard by law.

Management's Comment

We concur with the audit finding and recommendation. Compliance with the Financial Integrity Act is a priority for the Tennessee Regulatory Authority. A new internal audit team has been formed and discussions will be planned to develop audit goals and methodologies, deadlines for completion of audit phases, review procedures to ensure deadline compliance, and completion dates for reports to be submitted to Commissioner of Finance and Administration and the Comptroller of the Treasury consistent with state law. The team, comprised of CPAs and headed by the former Director of Internal Audit for the Department of Finance and Administration will perform the internal audit function. The team will be multi-divisional, within the agency, so that a workload crisis in one division will not significantly impair the internal audit function. The internal audit team will report directly to the Chairman.

PRIOR AUDIT FINDINGS

Section 8-4-109, *Tennessee Code Annotated*, requires that each state department, agency, or institution report to the Comptroller of the Treasury the action taken to implement the

recommendations in the prior audit report. The Tennessee Regulatory Authority filed its report with the Department of Audit on March 17, 1997. A follow-up of all prior audit findings was conducted as part of the current audit.

RESOLVED AUDIT FINDING

The current audit disclosed that the Tennessee Regulatory Authority had corrected a previous finding concerning inadequate controls over cash receipts.

REPEATED AUDIT FINDING

The prior audit report also contained a finding concerning the failure to comply with the Financial Integrity Act. This finding has not been resolved and is repeated in the applicable section of this report.

OBSERVATIONS AND COMMENTS

TITLE VI OF THE CIVIL RIGHTS ACT OF 1964

Tennessee Code Annotated, Section 4-21-901, requires each state governmental entity subject to the requirements of Title VI of the Civil Rights Act of 1964 to submit an annual Title VI compliance report and implementation plan to the Department of Audit by June 30, 1994, and each June 30 thereafter. For the year ended June 30, 1997, the Tennessee Regulatory Authority filed its compliance report and implementation plan on July 2, 1997.

Title VI of the Civil Rights Act of 1964 is a federal law. The act requires all state agencies receiving federal money to develop and implement plans to ensure that no person shall, on the grounds of race, color, or origin, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving federal funds.

The State Planning Office in the Executive Department was assigned the responsibility of serving as the monitoring agency for Title VI compliance, and copies of the required reports were filed with the State Planning Office for evaluation and comment. However, the State Planning Office has been abolished. The Office of the Governor is currently evaluating which office in the Executive Branch will be the new monitoring agency.

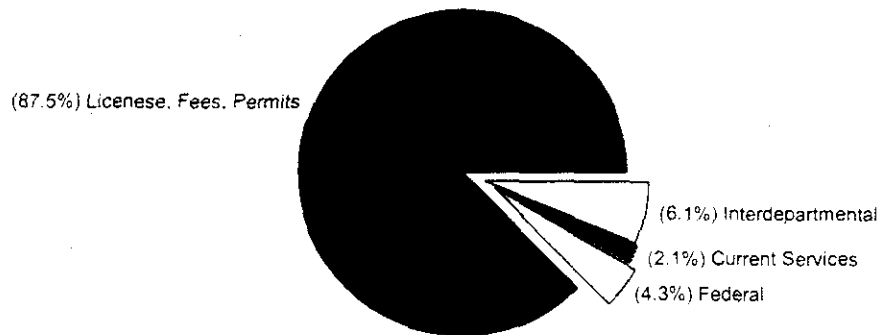
A summary of the dates state agencies filed their annual Title VI compliance reports and implementation plans is presented in the special report *Submission of Title VI Implementation Plans*, issued annually by the Comptroller of the Treasury.

APPENDIX

The Tennessee Regulatory Authority has one division and allotment code: 316.11.

Funding Sources

Fiscal Year Ended June 30, 1997 (unaudited)



Source: Tennessee Regulatory Authority